Supreme Court, U.S.
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No. 00-160

IN THE

Supreme Court of the United States

BRAZOS ELECTRIC POWER COOPERATIVE, INC.,

Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION
and TENASKA IV TEXAS PARTNERS, LTD.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

REPLY BRIEF

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PARTIES TO THE PROCEEDING AND CORPORATE DISCLOSURE STATEMENT

The parties below are those listed in the caption. Brazos Electric Power Cooperative, Inc. is an electric cooperative, which is owned by its member electric distribution cooperatives in Texas, which in turn are owned by those who purchase electricity from the cooperatives.

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I. This Case Presents The Important Issue Of When An Irrebuttable Factual Presumption Can Be Used To Establish A Statutory Prerequisite To An Entitlement In The Face Of Evidence Refuting That Presumption; This Is Not A Routine *Chevron* Case

FERC denies "that the Commission has employed an irrebuttable evidentiary presumption to avoid the statutory requirements of QF status," *viz*, whether the production of distilled water at Tenaska's Cleburne Plant was "useful." FERC Br. at 10. Rather, it claims to have adopted a permissible statutory interpretation of 16 U.S.C. § 796(18)(A), Pet. App. 71a, that steam used to produce a common product is *per se* "useful thermal energy . . . used for industrial, commercial, heating, or cooling purposes." FERC Br. at 10-11, *quoting* 18 C.F.R. § 292.202(c), Pet. App. 82a. It argues that its construction passes muster under *Chevron U.S.A., Inc. v. NRDC*, 467 U.S. 837 (1984). FERC Br. at 11. Contrary to FERC's argument, neither FERC decision below nor any other Commission order announces such a construction of the statute. FERC stated expressly that it was applying a "presumption" that was not rebuttable by Brazos' evidence, as the court below clearly understood. Moreover, even if FERC's order were based not on an irrebuttable presumption but on a construction of the governing statute and had been affirmed on that basis, the case would be worthy of *certiorari*.

A. FERC Has Applied An Irrebuttable Presumption

FERC stated below that because the use of steam to distill water is common, the Commission "presumes" or "assumes" that Tenaska's use of steam at the Cleburne Plant is useful within the meaning of PURPA, and, therefore, that it would not "look into the economics of [Tenaska's] sale of the product, or into how the product is being used by the unaffiliated purchaser of the product." Pet. App. 59a–62a. On rehearing, FERC amplified the point. Addressing Brazos' observation that past Commission decisions had conceded that a common use of thermal output is not necessarily useful, FERC responded not that Brazos'

challenge is contrary to the statute, as it would be if steam used to create a common product were useful by definition, but rather that "the statute *allows* our inquiry to end when, as here, a QF's use is shown to be common." Pet. App. 49a (emphasis added).

The court below clearly understood that FERC had applied a factual presumption, and just as clearly accepted that it could legally do so. The court conducted a careful review of FERC's precedents, Pet. App. 12a–17a, and concluded (at 14a): "Given the consistency with which FERC has denied further inquiry into common thermal applications, nothing in these precedents persuades us that FERC's presumption of usefulness is rebuttable, even post operation, by the two sets of facts Brazos presents." Even FERC's Question Presented admits that the issue is whether FERC "may *presume* that the thermal output of a cogeneration facility is 'useful'" in the context presented here (FERC Br. at (I), emphasis added).

FERC does not cite any language in its orders below to show that it interpreted PURPA to provide that, as a matter of law, "thermal energy used in a common commercial distillation process is useful" for purposes of PURPA, which is the proposition now advanced before this Court (FERC Br. at 10-12). Indeed, there is *no* FERC order to this effect. The only citation in FERC's brief for this proposition is to the leading case on the usefulness requirement, *Electrodyne Research Corp.*, 32 F.E.R.C. ¶ 61,102, at 61,279 (1985) (FERC Br. at 11). But *Electrodyne* holds that the statutory criterion of usefulness is an economic question. It does not state that all common uses of steam are *conclusively* deemed useful for purposes of PURPA; the order merely states that "common industrial or commercial applications are presumptively useful." *Id.*

FERC acknowledges, as it must, that in order to satisfy the statutory prerequisites for the receipt of QF benefits — to be "useful" — the thermal output "must have an independent business purpose with some economic justification." (Br. at 3, quoting *Electrodyne*, 32 F.E.R.C. at 61,278.) FERC continues by explaining that this policy is needed to "protect[ ] against

the extension of QF status to facilities that generate thermal energy solely in an effort to receive the regulatory benefits of QF status, without any independent business purpose or economic justification." (Br. at 3.)

Here steam was being used to produce millions of gallons of distilled water which was poured into sewers, using just enough thermal energy to meet FERC's minimum percentage for QF status during the Cleburne Plant's first 12 months of operation. Not only was the "price" paid for this water, $10 per month, clearly an amount far below the cost of producing 150,000 gallons of distilled water per day,[1] but Tenaska received *no* incremental revenues for *any* gallon it produced. Yet rather than reaching the obvious and inevitable conclusion that the thermal energy was being used solely "to receive the regulatory benefits of QF status, without any independent business purpose or economic justification," for the first time in the case of an operating generator FERC refused to examine whether there was any independent business purpose or economic justification for the use of steam to distill water. It did so, as it explains (Br. at 7, *quoting from* Pet. App. 62a) by *assuming* "that energy is useful within the meaning of the statute when it is used . . . to produce a common product."

FERC's substitution of the production of a common product for the statutory requirement that the product be produced for an industrial or commercial purpose — that there be an independent economic justification for the use of steam or thermal energy — is irrational. FERC's 1995 order certifying the Cleburne Plant as a QF cited *LaJet Energy Co.*, 44 F.E.R.C. ¶ 61,070 (1988), as a case that "clarified" the *Electrodyne* rule. *Tenaska IV Texas Partners, Ltd.*, 70 F.E.R.C. ¶ 62,026, at 64,081 (1995). And as FERC all but concedes, FERC Br. at 15-16, *LaJet* contradicts the construction of *Electrodyne* that FERC urges here, because *LaJet* holds that if an applicant for certification submits evidence suggesting that a facility's use

1. This average figure came from the City's public works director, who stated that he was unsure of it, as the City was not metering the deliveries. *See* C.A. App. 94.

of thermal energy to produce a common product for sale is *not* economically justified, FERC will consider that evidence, even if the thermal use is common and thus *presumptively* useful. 44 F.E.R.C. at 61,196.[2]

In sum, FERC's contention that its denial of the relief sought by Brazos without evaluating Brazos' evidence was predicated on something other than the application of an evidentiary presumption is not credible. FERC's orders and the decision of the court below all show that the Commission applied a presumption of usefulness not rebuttable by Brazos' factual allegations notwithstanding the relevance of those allegations under the statute.

FERC cites *Allentown Mack Sales & Serv., Inc. v. NLRB*, 522 U.S. 359 (1998), and *Fall River Dyeing & Finishing Corp. v. NLRB*, 482 U.S. 27 (1987), apparently to suggest that formulation of irrebuttable presumptions by administrative agencies is a permissible practice under settled precedent and does not warrant this Court's further attention. (FERC Br. at 12.) However, the presumption "recognized" in *Fall River Dyeing*, concerning a union's majority status during the year following its certification as a bargaining representative, is a direct outgrowth of a statutory provision. As this Court explained in *Brooks v. NLRB*, 348 U.S. 96, 101-02 (1954), the NLRB had employed a *rebuttable* presumption prior to the enactment in 1947 of 29 U.S.C. § 159(c)(3), which bars new elections for twelve months following certification. And the discussion of "counterfactual evidentiary presumptions" and categorical

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2. As *LaJet* shows, FERC's presumption of usefulness is not *always* irrebbutable. Instead, the rule first announced in *Bayside Cogeneration, L.P.*, 67 F.E.R.C. ¶ 61,290 (1994), and first applied in the post-operation context in this very case (*see* Pet. App. 15a), is that the *Electrodyne* presumption is not "rebuttable upon the submission of economic evidence *by a party opposing certification*," because FERC postulates that allowing an opportunity for trial-type evidentiary hearings on the usefulness of a common co-product would impede development of cogeneration facilities. 67 F.E.R.C. at 62,006 & n.5 (emphasis added).

exclusion of evidence "without reference to its inherent probative value" in *Allentown Mack*, 522 U.S. at 378, is an aside in a case that concerned the weight properly accorded to certain evidence and the appropriate standard of proof. In any event, *Allentown Mack* states that even "clearly announced" irrebuttable presumptions or rules of evidentiary exclusion "would of course be subject to judicial review for their reasonableness and their compatibility with the [governing statutes]." *Id.* In this case, FERC's application of the irrebuttable presumption to an operational plant is unprecedented. Pet. at 5-6; Pet. App. 15a.

Moreover, there is nothing reasonable about the notion that using a small fraction of the steam produced at an electric generating station to distill water necessarily has an independent business purpose and economic justification apart from obtaining QF benefits. Whether there is even a market for distilled water is dependent on such factors as degree of purity and transportation costs to a site with a need for water of the quantity and quality produced. All FERC knows, and under its irrebuttable presumption all that it will ever know, is that it has received a number of applications for initial QF certification proposing to distill water and, therefore, it has determined that production of distilled water by QFs is common. But, as Brazos has stated (Pet. at 22), and the briefs in opposition do not even attempt to challenge, for a given generator to produce distilled water requires merely a container filled with water under heat. The cost is low compared to the hundreds of millions of dollars of PURPA benefits made available by Congress to legitimate QFs. FERC properly recognized in *LaJet* that PURPA creates powerful economic incentives for a generator to install and operate a water distillation plant even where the plant would not be profitable on its own. And FERC's comment that "[n]o third party would buy the product of a thermal process if the thermal process were not useful" (FERC Br. at 10) is astounding here, where there is an obvious motive for Cleburne to agree to spend $120/year to buy unneeded water: assisting

Tenaska in obtaining and maintaining QF status so that it would build and operate a much-desired plant in that community.

FERC suggests that providing an opportunity for evidentiary hearings each time there is a substantial challenge to a cogeneration facility's compliance with the independent business purpose test "would seriously impede the very development of cogeneration and small power production that Congress sought to facilitate." Br. at 8, *quoting* Pet. App. 48a. But that assertion is blind to the distinction drawn by Congress between legitimate cogeneration products and those which serve no economic purpose other than to obtain PURPA benefits. Congress only sought to develop cogeneration that promotes energy efficiency by producing useful co-generated products, not "cogeneration" which, as here, wastes fuel. FERC's concern over the impact of granting "the opportunity for evidentiary hearings" is a quarrel with Congress and, indeed, with the rule of law.[3] FERC cannot use its presumption "to avoid the necessity for finding that which the legislature requires to be found." *United Scenic Artists, Local 829 v. NLRB*, 762 F.2d 1027, 1034 (D.C. Cir. 1985).

Even if FERC's presumption of usefulness were sufficiently rational to be allowable as a rebuttable presumption, Court review is warranted to explore when and under what circumstances an agency can adopt an irrebuttable presumption that permits parties to receive benefits at the expense of other parties without providing an opportunity for the disadvantaged parties to show that statutory requirements have not been met.

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3. There are a number of approaches FERC could consider to reduce the need for evidentiary hearings. One possible approach might be to grant safe harbors under certain circumstances to applicants who have business plans showing that they have legitimate prospects of profit on the co-generated product. If that approach is utilized, presumably, the entities providing the financing will demand review of the business plans and money will not be forthcoming without a proper plan. Another might be to establish *rebuttable* presumptions combined with expedited review procedures. Approaches such as these could be established in a rulemaking or other proceeding. However, FERC's task is to conform with — not negate — commands of Congress.

B. The Statutory Construction Advanced Here By FERC Is Worthy Of *Certiorari*

Should the Court elect to credit the dubious proposition that FERC refused to consider Brazos' evidence because FERC has determined for purposes of PURPA that all common co-products are *necessarily* useful, then this case still merits review. Admittedly, on this view the case would no longer give this Court an opportunity to give clear guidance as to when administrative agencies may establish irrebuttable evidentiary presumptions. However, the other reasons for granting the writ would remain: (1) the national economic importance of the statutory question presented and (2) the presence of a clear conflict with *Southern California Edison Co. v. FERC*, 195 F.3d 17 (D.C. Cir. 1999). They remain because there is no *practical* difference between saying that a common coproduct satisfies PURPA's usefulness requirement as a matter of law and saying that PURPA allows FERC to apply a *presumption* of usefulness that is not rebuttable by evidence submitted by an opposing party. Either way, the would-be cogenerator's entitlement to PURPA benefits is made unassailable.

There is no serious debate concerning the economic importance of the issue. PURPA gives generators leverage to negotiate power contracts at favorable rates and then screens those rates from review for "justness and reasonableness" by federal or state regulators. FERC observes that Brazos was under no obligation to contract with Tenaska because the Cleburne Plant had not yet been certified as a QF (FERC Br. at 5; *cf.* Tenaska Br. at 7, emphasizing "arm's length negotiations"), but the sequence is irrelevant because QF status was intended and, at least at the pre-operating stage, unquestionably available. And the Plant's QF status led the PUCT to dismiss Brazos' complaint before that body. (Tenaska Br. at 4, note 4.) Nationally, as noted in the briefs of *amici*, the cost of PURPA status to consumers is billions of dollars annually.

The conflict with *Southern California Edison* is also clear. There, FERC argued that to directly promote PURPA's statutory

purpose of encouraging energy conservation, it could adopt a construction of 16 U.S.C. § 796(17)(A)(i), Pet. App. 69a. that essentially read the word "solely" out of the statute. Here, FERC argues that to promote the statutory purpose of encouraging cogeneration, it may construe 16 U.S.C. § 796(18)(A), Pet. App. 71a, to eliminate the words "purposes," that is, the element of intent. PURPA does not dictate *what* a cogenerator must do with steam or heat not used to generate electricity so much as *why*. If PURPA spoke of a *process* rather than intentions then, as the court below recognized, a cogenerator could itself distill water with the intent of disposing of that water down the sewer. Pet. App. 22a. Yet FERC contends (Br. at 9) that it may permissibly construe the statute to bar inquiries into commercial intent because such inquiries could induce litigation, and the court below agreed. There is a clear and important conflict between two circuits on whether FERC may, purportedly to serve PURPA's broad goals, ignore express statutory limitations on eligibility for QF benefits.

II. The Dispositive Facts Of This Case Are Clear

Tenaska, for its part, attempts to muddy the facts in order to make this case appear inappropriate for Supreme Court review. Specifically, Tenaska contends that "FERC accepted Tenaska's representation that the $10 credit for distilled water was 'but one part of a multifaceted financial package' between Tenaska and the City, and thus found that commercial sales to a third party were in fact occurring." (Br. at 5.) In fact, as FERC's brief at 7-8 accurately reflects, FERC noted Tenaska's allegation but did not accept it, reasoning that under its presumptions there was no need to examine the economics of the sale to establish the legitimacy of the sale. *See* Pet. App. 47a–48a.

To the extent that there is any difficulty, it arises from the fact that the appeals court mistakenly believed that FERC had determined that the Distilled Water Supply Agreement was part of an "integrated financing package" (Pet. App. 12a), and proceeded to affirm the phantom finding, concluding: "Seen in the context of a complex project financing, Tenaska's

arrangement with the City garnered it more than ten dollars a month" (Pet. App. 18a). The factual problem with this line of argument is that, although Tenaska and Cleburne clearly do have a set of complex contractual arrangements involving financing, tax abatements, purchase of treated effluent and the like, Tenaska offered no evidence suggesting that the tax abatements, etc., were hidden payments for the distilled water. All record evidence is to the contrary.[4]

The posture of this case is that FERC, believing that it would contravene the purposes of PURPA to hold an evidentiary hearing on Brazos' claim that Tenaska had no *bona fide* independent commercial purpose for producing distilled water at the Cleburne Plant, denied Brazos' request for relief based on its presumption without investigating the facts. On judicial review, Brazos' allegations must be assumed to be true.

In addition to being improper and unfounded, the appeals court's belief that the distilled water sale was part of an integrated financing package is beside the point, because it does not address the critical question of whether Tenaska's use of steam to distill some 150,000 gallons of water per day during the twelve month period from September 1996 to August 1997 was for an independent commercial purpose. Irrespective of the larger context of the arrangements between Tenaska and Cleburne, it is uncontested that Tenaska received $120 under the Distilled Water Supply Agreement for all of the distilled water that it produced between September 1996 and August 1997. It is uncontested that Tenaska would have received this same $120 no matter whether it produced 60 million gallons of distilled water or *no* gallons of distilled water, and that the contract did not require Tenaska to produce any particular quantity of distilled water. Tenaska never alleged that other consideration

4. The best evidence is the Distilled Water Supply Agreement itself, which (1) contains an integration clause (¶ 19.D) that negates any contention that it is part of a larger arrangement, (2) is terminable by Tenaska at its discretion with thirty days' notice (¶ 3.B), and (3) does not require Tenaska to produce any minimum quantity of distilled water (¶¶ 1.A, 4) or even to make any effort to do so. C.A. App. 172-85.

it received from Cleburne was tied to the quantity of distilled water produced at the Plant. It is uncontested that the City had no use for any of this water, and that it all went down the sewer, because the City does not claim to have located a purchaser for the water until September 1997. Pet. App. 9a. Tenaska itself claims that during this twelve month period, it used 5.26% of the total energy output of the Cleburne Plant to distill water, C.A. App. 384-86, which, as it happens, exceeds by a small margin the 5% minimum established by FERC's regulations for qualifying cogenerating facilities. 18 C.F.R. § 292.205(a)(1), Pet. App. 85a. And, finally, it is uncontested that at least some of the fuel used to make this steam, and perhaps all of it, *could have been used* to generate more electricity instead of distilling more water. The question that this case presents is whether, under these facts, FERC may *presume*, or otherwise hold without weighing Brazos' evidence, that Tenaska's use of all this steam (or indeed any of it) during those twelve months to make distilled water was for a commercial purpose independent of Tenaska's desire to qualify for PURPA benefits.

CONCLUSION

This case is worthy of review because it calls into question parties' most basic rights to have their cases decided based on evidence, not on an irrational, irrebuttable presumption. When the production of distilled water that is dumped down the sewers can give rise to hundreds of millions of dollars of benefits, and when millions of gallons of distilled water were deemed distilled for a commercial purpose despite a contractual obligation to "sell" any such water for no incremental compensation, something is wrong. As is set forth in Brazos' petition for *certiorari* and in the briefs of *amici curiae*, the cost to ratepayers nationwide of power contracts insulated from state and federal regulatory scrutiny by PURPA is enormous, and there is a pressing need to correct FERC's determination below that it will not hear challenges by purchasers of overpriced power under such contracts to the statutory propriety of those PURPA benefits. The writ should be granted.

Respectfully submitted,

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